



REPORT OF THE FINANCE COMMITTEE

March 24, 2015

BUDGET OVERVIEW

The proposed total spending for Town operations (Article 5) is \$26,900,419 for FY2016, an increase of 3.3% over FY2015, including the Town's contribution to the School Department. In the discussion below we provide an analysis of both Government's and the Schools' numbers.

The proposed budgets for the Water and Sewer Enterprise Funds (Articles 5A and 5B) total \$3,484,590, an increase of \$9,399 from last year. These funds are covered solely by water and sewer user fees and therefore, are separate from the main operating budget and do not affect the tax rate.

The proposed Capital Spending Items, Articles 6, is \$1,104,691. The proposal for the Enterprise Funds, Articles 6A and 6B, totals \$130,000.

In the discussion below we provide an analysis of the departmental expenses, capital outlay, revenue and financial issues in the proposed budget.

KEY FINANCIAL ITEMS FOR VOTERS

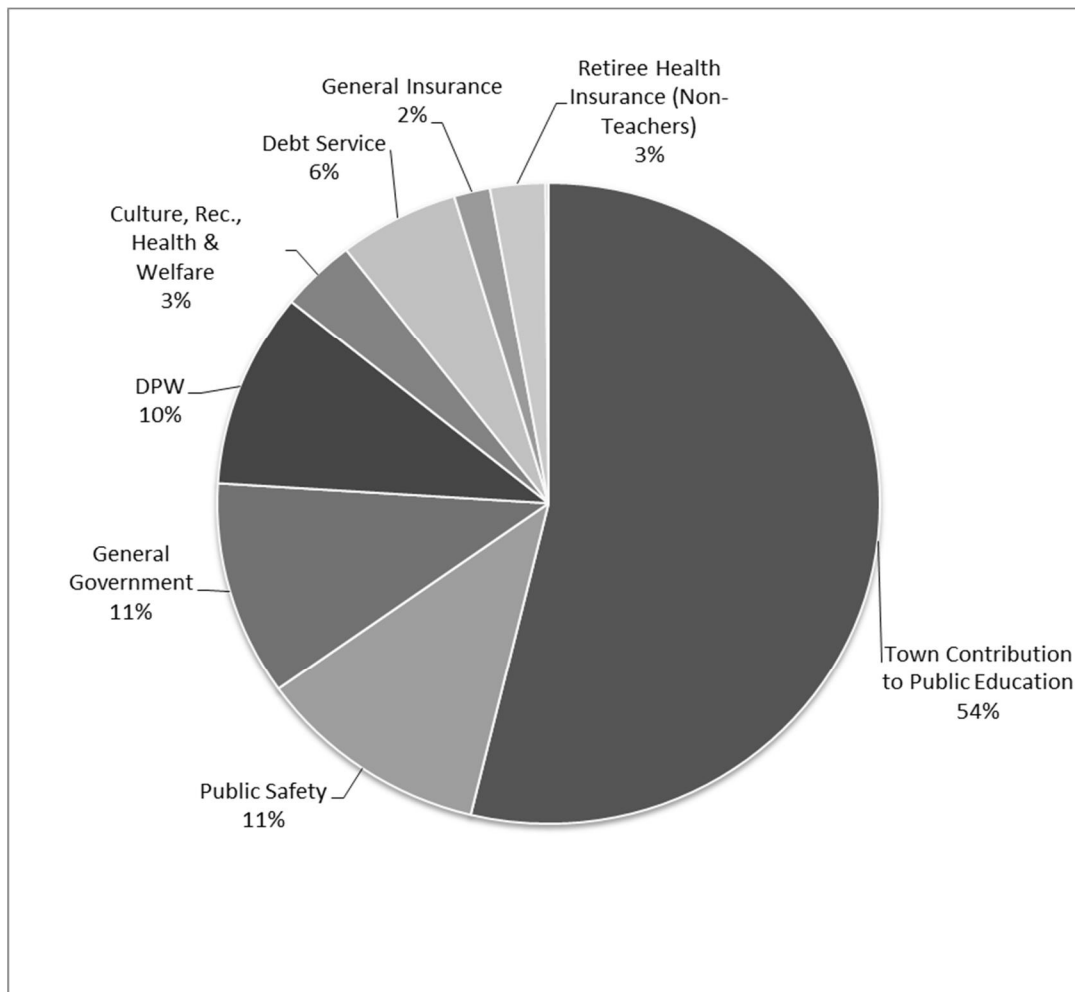
In addition to the normal requests for approval of routine budget items, there are a few key items for voters to understand this year:

1. The proposed budget includes an increase of 2.3%, or about \$240,000, in the direct appropriation to the School Department, in line with the school proposal last spring. The School Committee in turn has approved a budget with an increase of less than 3%.
2. Tax supported debt service is increasing by about \$215,000, and Water & Sewer debt service is increasing by \$65,000.
3. Payments for Health Insurance and Pensions will increase by about \$400,000 in FY2016. Without a complex restructuring of benefits, we expect these to continue to increase substantially in the future.
4. The budget includes an increase of \$60,000 for the new financial management system.
5. Mostly because of the increases above, the Finance Committee is recommending an operating budget that includes cuts from the departmental requests of about \$340,000.

OPERATING BUDGET HIGHLIGHTS

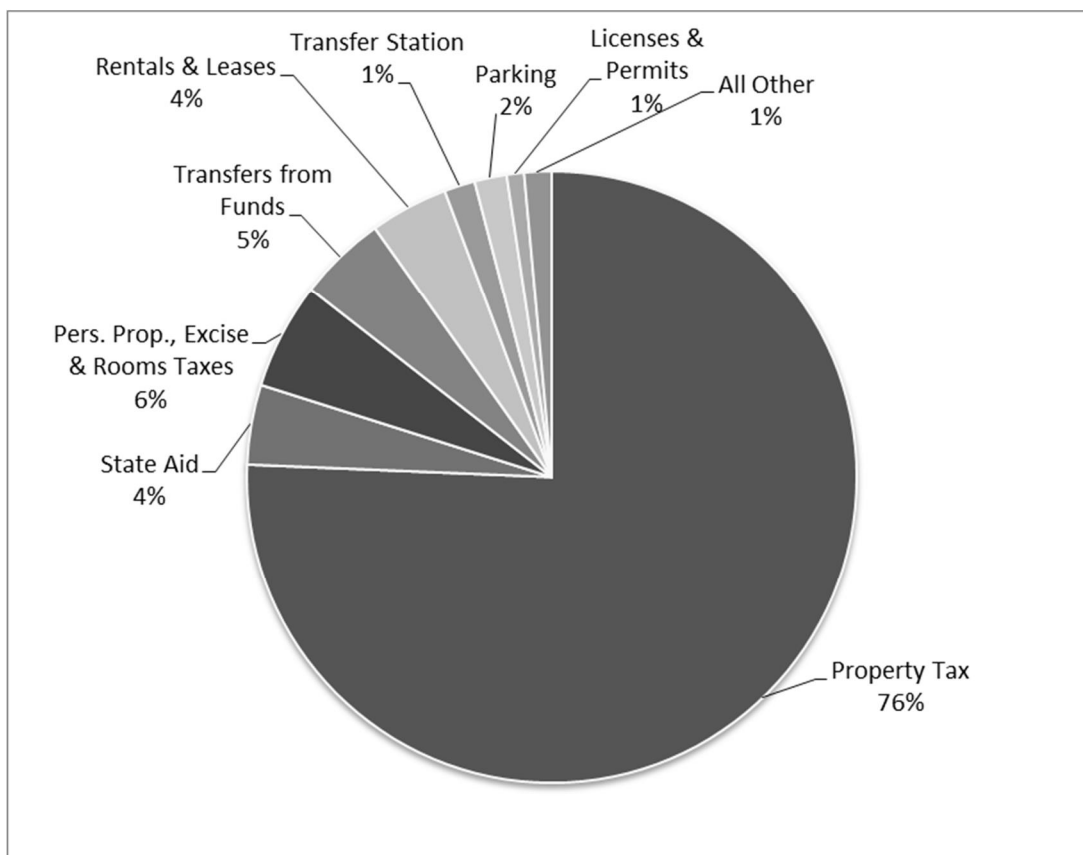
The numbers below show summaries by categories. They represent the total spending of the departments plus the full allocation of employee benefits attributable to each. We restated the numbers this year so as not to allocate debt service payments to each individual department. We thought that the allocation added to complexity without usefully describing the departments' expenses. In the case of the Schools, the amounts below represent only the Town's contribution. The Schools also receive state and federal grants as well as other monies.

Total Operating Expenses		
	2015	2016
Town Contribution to Public Education	\$ 14,067,742	\$ 14,466,462
Public Safety	\$ 3,035,202	\$ 3,066,771
General Government	\$ 2,869,589	\$ 2,909,414
DPW	\$ 2,478,609	\$ 2,650,528
Culture, Rec., Health & Welfare	\$ 995,306	\$ 992,179
Debt Service	\$ 1,361,584	\$ 1,575,949
General Insurance	\$ 457,810	\$ 474,850
Retiree Health Insurance (Non-Teachers)	\$ 689,742	\$ 726,091
Unallocated Expenses	\$ 78,660	\$ 38,176
Total Budget - Article 5	\$ 26,034,242	\$ 26,900,419



State law requires that the budgets of cities and towns in the Commonwealth be balanced. Revenue sources must be equal to or greater than budgeted spending. The table below shows revenues that are generated locally by the Town or aid that is provided by the state to offset some of the costs. These revenues contribute to decreasing the costs the Town is required to raise from property taxes.

Revenues		
	2015	2016
Property Tax	\$ 19,521,379	\$ 20,351,227
State Aid	\$ 1,073,387	\$ 1,132,279
Pers. Prop., Excise & Rooms Taxes	\$ 1,451,094	\$ 1,521,000
Transfers from Funds	\$ 1,310,429	\$ 1,249,381
Rentals & Leases	\$ 895,470	\$ 1,112,399
Transfer Station	\$ 410,000	\$ 438,305
Parking	\$ 414,166	\$ 458,749
Licenses & Permits	\$ 245,978	\$ 246,670
All Other	\$ 420,070	\$ 390,409
Total Non-Tax Revenue & State Aid	\$ 6,220,593	\$ 6,549,192
Total Revenue	\$ 25,741,972	\$ 26,900,419



There are several items in the revenue figures above that should be noted:

1. There are three components of the increase in Property Tax revenue. One is the increase in taxes on existing housing stock, which is limited to 2.5%. Secondly, the tax levy may be raised by overrides or debt exclusions. Third, there are taxes based on "New Growth" which is the additional assessed value of new or renovated properties.
2. Parking Revenue above consists of parking sticker revenues, parking fines and withdrawals from the parking meter fund. The new meters last year failed and were replaced by the old meters in August. We expect that new meters will be in place for this year's season, and that they will increase meter revenues. This increase

will be available for the FY17 budget. The fee for parking stickers will be increased this year, and those increased revenues are included in the revenues above.

3. Rentals and Leases consist primarily of Long Beach and cell tower leases. The Town owns the land under the cottages on Long Beach, for which the Selectmen recently executed new 10-year leases. Under the new leases rental revenue will increase about \$150,000 per year.
4. Some examples of Fund Transfers & All Other are expense reimbursements from the Enterprise Funds, Ambulance Revenues and Mooring Fees.

PUBLIC EDUCATION

The Finance Committee recommends that \$10,964,411 be authorized in Article 5 for support to the Schools' operating budget. On the chart of numbers below, you can see that other costs of the school system, Debt Service and Pensions & Benefits totaling \$3,186,555, are expenses paid directly by the Town. In addition, the Town is assessed \$315,497 for Essex Technical High School where 15 Rockport students attend. The total of these items above is \$14,466,462 which the Town would provide. At the bottom of that chart, you can see that we expect the state and federal governments to reimburse the Town, Chapter 70, \$1,393,521 for these expenses. Thus, after adjusting for School Choice Sending and Medicaid Assistance, the Town taxpayers would be responsible to pay a net amount of \$13,185,656 for its schools.

Here we will analyze the total school operations including all expenses and sources of revenue. The total school expenses proposed for this year are \$16,360,656. As mentioned above, the Town provides \$14,466,462 of this. In addition, the Schools are able to source \$1,846,455 independently from the Town. These revenues largely come from School Choice, Fees, and State and Federal Grants.

Under state law, the School Committee has control of the entire budget after the Town contributions are voted by Town Meeting. To assist the voters of Town Meeting to better understand the financial situation of the schools, we are providing the following analysis. This analysis itemizes all expenses and sources of revenue regardless of who controls them. In the current year, FY15, the Schools are responsible for educating 984 students, 760 of whom are Rockport residents.

Expenses: Listed below are all expenses associated with educating the students. When reading these items, please refer to the table below.

1. Most of the day-to-day expenses are comprised of Labor and Operating Expense, which are \$10,327,036 and \$825,553 respectively. These categories also include the expenses of educating SPED students who remain in our schools.
2. Some SPED students need more specialized instruction than can be provided by our school system. These expenses are designated as SPED Outside Services, and are budgeted by the School Committee to be \$1,706,016.
3. When analyzing the total cost of the schools, we allocate the cost of debt service for school-related borrowing, \$228,032; the cost of Pension & Benefit expenses of current employees, \$2,532,809; and the cost of retired teachers, \$425,713 to the schools. These costs are paid directly by the Town's General Fund.
4. Some Rockport students attend Essex Technical High School. The expenses of \$315,497 are shown in the chart below as a school expense paid by the Town.

Sources of Revenue: As mentioned above, not all of these expenses are paid by the Town's taxpayers. We have identified two types of school revenue as can be seen in the chart below.

1. Town Contributions:

- a. As outlined above at the top of this section, we recommend that the Town provide a total of \$14,466,462 in Article 5.
- b. We also recommend that the ATM voters approve \$64,755 from Free Cash to fund certain capital outlays in Article 6.

2. Independent Revenue:

- a. \$1,218,900 in School Choice Receiving – The Rockport School Committee agrees to a certain number of openings in each class that are available for Choice students. The Schools receive approximately \$5,500 per student from the sending school system when their students opt to go to the Rockport schools.
- b. \$298,555 in Circuit Breaker - The State reimburses Rockport's schools for a percentage of the most extraordinary individual special education expenses it incurs above a threshold amount.
- c. \$275,000 in expected Grants - The Schools receive a number of grants which offset some of the costs of delivering specific education programs and initiatives.
- d. \$54,000 in athletics and transportation fees.
- e. In addition, the School Committee can use reserves to cover additional expenses. They estimate that their reserve balances will be \$844,000 at the end of FY15.

Rockport Public Education		
Revenue	FY15	FY16
Town Contributions:		
Base Funding - ATM Appropriation	\$ 10,727,560	\$ 10,964,411
Debt Service (700)	\$ 215,884	\$ 228,032
Pensions & Benefits (900)	\$ 2,382,201	\$ 2,532,809
Retired Teacher Health Insurance	\$ 425,820	\$ 425,713
Essex Technical High School	\$ 306,280	\$ 315,497
Total Town Contributions	\$ 14,057,745	\$ 14,466,462
Independent Revenue:		
School Choice	\$ 1,167,443	\$ 1,218,900
Circuit Breaker	\$ 298,555	\$ 298,555
Grants	\$ 275,000	\$ 275,000
Fees	\$ 75,000	\$ 54,000
Total Independent Revenue	\$ 1,815,998	\$ 1,846,455
Total School Revenue	\$ 15,873,743	\$ 16,312,917
Expenses		
Labor	\$ 9,955,131	\$ 10,327,036
Operating Expense	\$ 817,826	\$ 825,553
SPED Outside Services	\$ 1,713,916	\$ 1,706,016
Needed to Operate - Direct Expenses	\$ 12,486,873	\$ 12,858,605
School Expenses Paid by Town (see above):		
Debt Service (700)	\$ 215,884	\$ 228,032
Pensions & Benefits (900)	\$ 2,382,201	\$ 2,532,809
Retired Teacher Health Insurance	\$ 425,820	\$ 425,713
Essex Technical High School	\$ 306,280	\$ 315,497
Total Other Expenses	\$ 3,330,185	\$ 3,502,051
Total School Expense	\$ 15,817,058	\$ 16,360,656
Note: The Town receives Chapter 70 from the State, and Medicaid payments from the Federal Government. It pays School Choice Sending.		
Total Town Contributions (from above)	\$ 14,057,745	\$ 14,466,462
Less Chapter 70 Reimbursement	\$ (1,377,981)	\$ (1,393,521)
Less Medicaid Assistance - SPED	\$ (45,000)	\$ (50,000)
School Choice Sending	\$ 154,605	\$ 162,715
Funded from Tax Levy	\$ 12,789,369	\$ 13,185,656

The Finance Committee worked closely with the school department and the School Committee to adequately fund the Schools at a level affordable to the Town. Accordingly, the Finance Committee recommends Base Funding \$10,964,411, or 2.3% more than last year. The Schools kept their overall spending increase to 3%. In addition, since Special Education (SPED) expenses are very hard to control because of state regulations, last year Town Meeting voted to set up a SPED stabilization fund to cushion the impact of substantial swings in these expenses. If actual SPED expenses exceed the budget, the Schools may draw from this fund, and if they are less, they are required to deposit

the savings into the fund. We are happy to note that in the first year, the SPED expenses were \$15,344 less than the budgeted amount. The School Committee will request, and the Finance Committee will recommend, that this amount be deposited into the SPED Stabilization Fund by the Schools.

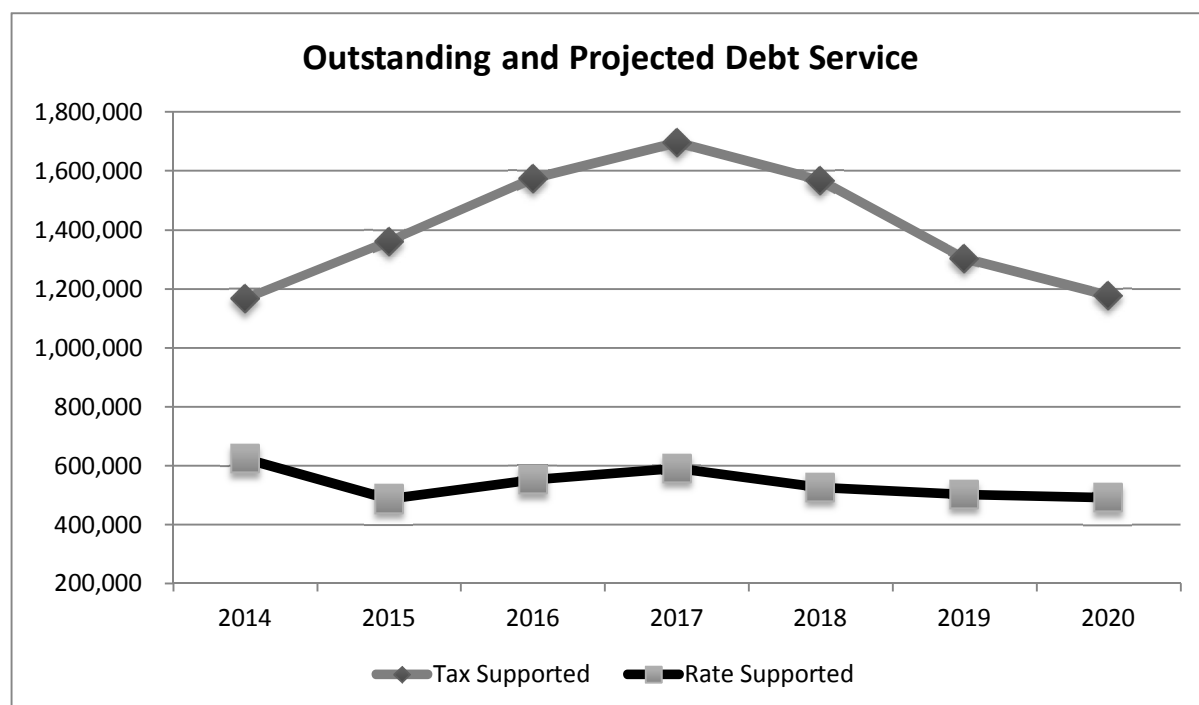
ENTERPRISE FUND HIGHLIGHTS

The Water & Sewer Enterprise Funds each operate separately from the Town's operating budget. These expenses are covered by water and sewer rates billed to the users, and thus do not affect the tax rate.

Enterprise Fund Budget Expenses		
	2015	2016
Water Fund - Article 5A	\$ 1,671,645	\$ 1,661,584
Sewer Fund - Article 5B	\$ 1,803,547	\$ 1,822,646

CAPITAL OUTLAY EXPENDITURES (ARTICLE 6, 6A AND 6B)

The Capital Improvement Planning Committee (CIPC) receives requests for capital items from the operating departments and the enterprise funds. It meets with each department and then prioritizes the requests before making a recommendation to the Board of Selectmen and the Finance Committee. Once the Finance Committee decides what it wants to recommend, it presents these articles to Town Meeting. Looking ahead, there are a number of large projects that will need to be addressed. These include Town building repairs, Old Harbor dredging, heavy equipment for the DPW, roadway upgrades, replacement of the DPW shed and numerous waterfront projects as they become necessary. The Town will need to control expenses, find additional non-tax revenue, borrow money, and increase taxes temporarily with debt exclusion overrides to meet these needs. The chart below shows tax supported debt service rising in FY16 and FY17 by a total of \$335,000 as a result of projects previously approved and in progress. Rate supported debt service rises by \$105,000 over the same two years.



UNFUNDED PENSIONS AND BENEFITS & OTHER FUTURE REQUIREMENTS

There are two significant categories of unfunded liabilities that the town must eventually address. The longer we wait, the more difficult it becomes to deal with these:

1. Retirement Fund. The town is part of the Essex Regional Retirement System which includes 19 towns and several dozen regional schools and authorities. Its auditors have determined that the system is underfunded by \$315 million as of December 31, 2013. Rockport's share is 5.33% or \$17 million, so we can expect that our payments will be increasing significantly over the next twenty years. In 2014, 2015 and 2016 fiscal years, our bills from ERRS have been \$1,222,458, \$1,376,414 and \$1,493,687 respectively. These are funds set aside to fund future retirement payments to both active and retired employees. Retirement payments are important for Rockport's employees because municipal employees are not eligible to be part of the Social Security System, and will receive no payments from it. Rockport does not have control over the funding level or the investment policy of the ERRS. It does, however, have the ability to review the level of retirement benefits of our employees.
2. Other Post Employment Benefits (OPEB). These are primarily health insurance benefits to retirees and their spouses. The annual cost of this set of benefits is included as part of the health insurance expense in the operating budget. As is the case with retirement benefits, these are obligations of the town, and will be paid on behalf of our retirees for many years into the future. We believe the state will require that the expected future costs be included as a liability on the Town's balance sheet soon. In their most recent report, our auditors calculated that our unfunded liability was \$29.5 million as of 7/1/2012. This compares to the current balance in the OPEB fund of \$232,033. This may become an issue for our debt rating. The Town has operated under a "pay as you go" philosophy, only funding the actual premiums for current retirees. No strategy has been formulated for current funding of future liabilities for current and future retirees. As it stands today, these payments will increase as our retirees live longer and as health insurance premiums rise. This has the potential to grow significantly, and possibly reduce the town's ability to fund other expenses or require additional tax increases. Rockport must work to control the growth of health insurance, and as a result, OPEB.

STABILIZATION FUNDS

The town has three funds to help it cope with future uncertain needs.

1. Stabilization Fund - \$1,390,663
2. Capital Reserve Stabilization Fund - \$175,424
3. SPED Stabilization Fund - \$200,000

Except for the small deposit from the schools into the SPED Fund, we are not in a position to recommend deposits into the first two above or to the OPEB Fund.

YOUR REAL ESTATE TAX BILL

There are several factors that go into the determination of your real estate tax bill:

1. The amount of spending in the operating departments;
2. Plus the retiree pension and health insurance payments;
3. Plus debt service;
4. Less the amount of local revenue (other than real estate tax);

5. Less the amount of state aid.

The result is the amount of the real estate tax levy for the Town as a whole. Under Proposition 2½, this levy is limited to:

1. Last year's levy limit plus 2½% growth;
2. Plus additions to the levy known "new growth" which are generated when a house is new or significantly renovated causing an increase in assessed value and, thereby, creating an increase in the tax base;
3. Plus any Proposition 2½% overrides previously approved by the voters.

Once the year's levy is established, the tax rate is determined by dividing the levy by the total assessed value of the Town's taxpayers' real estate. Therefore the change in the tax rate is determined by both the change in the levy and the change in the total assessed valuation. The resulting tax for your property is the product of its assessed value and the tax rate. In any year, the change your property's assessment may differ from that of the average property in town. If so, the percent change in your tax bill will differ from that of the average property in town.

For FY15, the total assessed value of Rockport's real estate was \$1,787,449,100. To raise the \$19,661,940 that was billed this year, the rate of \$11 per thousand was required. Therefore, a house assessed at \$500,000 would pay \$5,500.

FREE CASH

The Town has \$890,654 available Free Cash in the General Fund. Because this amount varies greatly from year to year, the Finance Committee supports using it for one-time capital expenditures, for one-time emergency payments and for building up our reserves rather than for funding on-going operating expenses. By using Free Cash for capital outlay, the Town is able to limit additional borrowing. The Finance Committee recommends using \$297,565 to finance Article 6 Capital Outlay items, \$120,000 to fund computer equipment under our five-year plan, \$25,000 to fund the Economic Development Committee and \$88,100 to support Special Articles in the 2016 ATM Warrants. The unspent balance of Free Cash of \$359,989 can be used for reserves and unforeseen expenses until our tax rate for FY16 is established later this year. Anything left over will be available as free cash for FY17.

The Free Cash of the Enterprise Funds totals \$166,158 (\$60,704 Water & \$105,454 Sewer). The Finance Committee recommends using \$60,000 and \$70,000 respectively to finance Articles 6A (Water) & 6B (Sewer) Capital Outlay items.

BUDGET UNCERTAINTIES

State Aid has been level funded, based on the Governor's proposed FY2016 budget, released on March 4th. Statewide, the Governor asks for increases in Chapter 70 aid to public K-12 education of 2.4% and increases in non-education Local Aid of 3.6%. The actual increase for the Town of Rockport may be less. Final State budgets are not adopted until after our Annual Town Meeting and adjustments to our budget will be made at the Fall Town Meeting.

By state statute and Town By-Law, the Finance Committee works directly for you the voters. We are charged with providing you with the best possible information so that you can make informed decisions. We hope you find it so.

The Finance Committee wishes to thank all the Town of Rockport's staff and volunteers for their diligence and patience throughout this year's budget process. Their dedication to the citizens of Rockport in maintaining and improving services is truly appreciated.

We also wish to thank all those who contributed directly to the preparation of this document.

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